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SUBJECT: HEDGING YOUR BETS: GERMANY LEANS TOWARDS NABUCCO,
BUT DOESN'T RULE OUT SOUTHSTREAM

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Classified By: MINISTER-COUNSELOR FOR ECONOMIC AFFAIRS ROBERT POLLARD
for reasons 1.4 (b,d).

11. (C) Summary: Germany demonstrated its growing support for the Nabucco gas pipeline by sending Economics Ministry heavyweight State Secretary Bernd Pfaffenbach to last week's Nabucco Summit in Budapest. During and after the conference the German government expressed guarded optimism regarding Nabucco, while privately RWE and government representatives sounded increasingly confident in the pipeline's chances. German officials, however, have also spoken out in favor of the Russian-proposed alternative to Nabucco (Southstream), demonstrating that the government remains acutely aware that its long-term dependence on Russia for energy means it needs to approach Nabucco in a manner that does not ruffle Russian feathers. End Summary.

12. (SBU) The January 27-28 Hungary-sponsored meeting on the Nabucco Pipeline in Budapest brought together the members of the Nabucco consortium (Austria, Bulgaria, Germany, Hungary, Romania, and Turkey) with its potential suppliers (Azerbaijan, Egypt, Iraq, Kazakhstan, and Turkmenistan), as well as other interested parties (the U.S., Georgia, Russia, and the EU). The German delegation was headed by Economics Ministry State Secretary Pfaffenbach. State Secretary Jochen Homann was originally scheduled to represent Germany, but bowed out because of a "conflict." While Homann is responsible for energy in the Economics Ministry, Pfaffenbach - who is close to Chancellor Merkel - is considered more of a heavy hitter, and his attendance is a sign of the importance Germany attached to the conference.

Germany More Supportive of Nabucco

13. (U) On 27 January, Pfaffenbach told the press that Germany welcomed what he characterized as emerging broad political support for Nabucco, emphasizing its significance as an alternative gas supplier. On the same day, Economics Minister Glos repeated his assessment that "the gas crisis has done visible damage to Russia's reputation as a reliable supplier and Ukraine as a reliable transit country." Chancellor Merkel has made similar public statements. The shock of the Gazprom cut-off clearly heightened German interest in Nabucco (reftels A-C).

But Merkel Says Germany also Supports Southstream

14. (SBU) Following the Budapest Conference, however, Chancellor Merkel wrote a letter to EU Commission President Barroso and current EU President Topolanek that presented a

confusing message by lumping the three pipeline projects together. Her letter called for all EU partners to back the Nordstream pipeline, as well as Nabucco, and Southstream. Furthermore, she threw cold water on an EU proposal to provide funding to Nabucco. The EU proposal called for spending 3.5 billion Euro of stimulus package funds on energy projects, including 250 million Euro for Nabucco, with Germany footing 1 billion Euro of the cost. Writing that "additional funds from the EU budget will not solve our problems," Merkel called on energy corporations to bear the costs.

More Light on the German Position

¶15. (C) In a 2 February meeting with ECONCOUNS, MinEcon's Deputy Director General for Energy Hartmut Schneider, who accompanied Pfaffenbach to Budapest, noted that the German Government supports Nabucco, but will not accede to RWE pressure and sign the Intergovernmental Transit Agreement(IGA) for Nabucco Transit countries. The complexity of this agreement, spelling out the conditions for transit of the pipeline through various countries, is one of the problems delaying completion of a Nabucco agreement. Schneider confirmed that while RWE is a member of the consortium, Germany is not a transit country, as the pipeline will end in Austria, and therefore cannot sign the IGA.

¶16. (C) Schneider observed that most Budapest participants were convinced that Nabucco would really start to move this year. While Germany appreciated the USG's strong support for Nabucco, including direct approaches to potential Caspian suppliers, it remained uneasy with the U.S. depiction of Nabucco as a counter to Russian domination of European energy supplies. Schneider was confident that gas supplies would be found for Nabucco, with Azerbaijan and Turkmenistan showing more willingness and flexibility. In his view, however, the Turks remained a problem as they had still not given up their demand for a 15 percent share of Nabucco gas for domestic consumption.

RWE is Also Encouraged

¶17. (C) In recent conversations with EMIN, RWE Representative Neil McMillan, who like Hartmut Schneider attended the event, emphasized that his company was also encouraged by the Budapest Conference outcome. Although the speeches were generally "very encouraging," he felt that the conference sent a clear message that the Intergovernmental Transit Agreement (IGA) needed to be sorted out quickly. McMillan was particularly pleased that the European Investment Bank (EIB) representative at the conference offered to provide both funding and regulatory expertise to the project.

¶18. (C) According to McMillan, the presence of State Secretary Pfaffenbach demonstrated Germany's growing support for Nabucco. At the conference Pfaffenbach reportedly noted Germany's growing reliance on Russia for its gas (currently 37 percent). As the EU clearly needed more pipelines and more energy sources, Pfaffenbach contended, Germany supported the construction of both Nordstream and Southstream. His comments reinforced statements made by McMillan and RWE Managing Director Stefan Judisch to the Charge prior to the Budapest Conference that the German government has become more supportive of Nabucco in the aftermath of the Ukrainian/Russian gas dispute (Reftel D).

Comment

¶19. (C) There has been considerable speculation in Germany that the just-concluded Ukrainian/Russian gas dispute could push Germany towards a change in its energy policy. Observers, therefore, closely examined the Budapest conference searching for clues. Public and private statements by RWE and Germany government officials indicate that Germany is now more aware of the need for alternative energy

sourcing, notably, the Nabucco pipeline. However, the German government is also acutely aware of its dependence on Russia for energy and is unwilling to be too far out in front of the EU. As a result, government statements have couched support for Nabucco in vague terms, burying it within a general statement of support for all pipelines, even Southstream, which is a Nabucco competitor favored by Russia. This did not prevent RWE from taking encouragement from the conference, which it viewed as bringing the realization of the pipeline one step closer. In the end, one factor has not changed: the German government still expects private companies to bear the brunt of financing Nabucco and other pipelines.

Koenig